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SUBJECT: U.S.-THAILAND FTA: STATUS AND PROSPECTS

#### SUMMARY

11. (SBU) The November 22 announcement by the Thai lead negotiator that the RTG was seeking a postponement of the December 2004 FTA round was the culmination of several complex crosscurrents within the RTG and Thai society. The ostensible reason for the postponement, the upcoming (February 6) elections, is genuinely believed by some senior officials, as is the need for additional time for preparation, but is probably the least important element of the whole story. Key elements within the RTG are dissatisfied with the comprehensiveness of the U.S. negotiating framework, particularly its inclusion of labor, environment, and financial services, as well as the emphasis on negative lists in services and investment. Key private sector organizations, notably the Thai Bankers Association, also have voiced their objections to U.S. requests. The prospective U.S. offer has disappointed some here, especially in areas such as temporary entry. The RTG currently is split into two camps on how to proceed: the first, led by Finance Minister Somkid and Chief Economic Adviser Pansak, argues for a go-slow, narrowly focused market access agenda; the second, led by lead FTA negotiator Nitya (who is allied with Foreign Minister Surakiart), favors a faster, more comprehensive approach, arguing that such an FTA would transform and modernize the Thai economy. They also stress the high costs of non-participation as other countries pursue FTAs with the U.S.

12. (SBU) Resolution of this debate awaits the February elections. Our opportunity for input is limited, although we may be able to make our negotiating framework more attractive here by emphasizing benefits to small and medium sized enterprises, a politically favored sector of the Thai economy. In spite of the delay and internal RTG soul-searching, we remain basically optimistic about the FTA's prospects because we don't see how either side's fundamental interests in having an FTA have changed. For the U.S., it is our best chance to maintain a favored trading and investment position with Thailand that is jeopardized by several imminent developments. Equally important, an FTA will be transformational for Thailand, effecting a shift in many of its governmental institutions towards a more rules-based economy. That will be good for Thailand, good for the U.S., and will serve as a positive precedent for the many other developing economies which are weighing economic development and trade policy options. In asking for a comprehensive, transformational FTA with the U.S., we are asking Thailand to do something unprecedented, something that it will find very hard. Negotiations are likely to take some time. Progress could prove non-linear, with periods of rapid movement forward, followed by some regression, a hiatus, and repetitions of this cycle. It will require patience, determination, and judgment, with no guarantee of success. But we believe it is worth the considerable effort likely to be required. End Summary.

#### FTA TALKS PUT ON HOLD

13. (SBU) On November 22, the RTG's chief negotiator announced that his government was proposing to the USG that the FTA negotiating round scheduled for the week of December 13 be postponed. The reasons he cited for the request were the upcoming Thai national elections (currently scheduled for February 6, 2005), and the need for additional time to prepare for further talks with the U.S. This announcement was pursuant to a decision made the previous day by the RTG's newly created FTA Oversight Committee. In addition to the postponement request, the Committee ordered the relevant agencies to further study the major issues in the FTA and provide recommendations on a future course of action.

14. (SBU) While the explanations publicly provided by the lead RTG negotiator are undoubtedly genuine, no one here believes they represent the complete story -- or even the primary story -- behind the postponement request. Rather, the postponement was the culmination of several complex crosscurrents within the RTG and Thai society.

#### THE ELECTIONS

15. (SBU) Prime Minister Thaksin's Thai Rak Thai Party and its

allies have gone into full campaign mode for the February 6 national elections, and all other issues are being viewed through the election prism. It is an unfortunate fact that public sentiment concerning Thailand's several free trade initiatives is almost entirely negative. Perhaps the most talked about trade deal is Thailand's "early harvest" tranche of the ongoing FTA talks with China. While the early harvest provisions contain significant benefits for prospective Thai exporters to China, press coverage has centered almost entirely on increased imports of Chinese onions and garlic, and resulting depressed prices for Thai farmers in this sector. (We have yet to see a mass media article that mentions any increase in consumer welfare due to lower food prices.)

16. (SBU) Against this backdrop, the U.S.-Thai FTA talks are regarded by the RTG as a potential political liability best avoided in an election campaign. From the perspective of the RTG, the only way the FTA talks with the U.S. could have been a useful campaign tool would have been an early harvest component which contained some attractive market access improvements for Thai exporters. The U.S. preference for a single undertaking that addresses substantially all trade and investment barriers meant that there would be no pre-election "presents" for Thailand (and the Thai Rak Thai party). Once that fact was recognized by PM Thaksin and the relevant RTG ministries, support for a pre-election negotiating round largely evaporated.

17. (SBU) But we don't accept the claim that the postponement request is all about -- or even primarily about -- an exogenous factor like the elections. For one thing, trade policy, while recently controversial and a political negative, is not a big vote-mover here. Many issues overshadow it. For another, Thailand's FTA talks with Japan are about as controversial here as those with the U.S., and yet the previously scheduled FTA talks with that country, scheduled for the week of December 6 in Bangkok, have gone ahead (and with very little media scrutiny). We doubt the December 13 FTA talks with the U.S. in remote Hawaii would have generated much in the way of media attention here.

#### NEED FOR ADDITIONAL PREPARATION TIME

18. (SBU) There is no question that the RTG has found itself ill prepared for negotiations with the U.S. The belated formation (in early November, five months after the start of negotiations) of the RTG's FTA Oversight Committee (chaired by Finance Minister Somkid) is, in part, a belated recognition that more work on positions has to be done, especially in (but not limited to) labor, environment, and financial services (the Committee's creation is also partly motivated by internal power struggles within the RTG -- para 15). One of our working level contacts in the Ministry of Commerce said, "If you look at the guys on our (the RTG's) labor and environment teams, you can see right away that they are not prepared to negotiate anything." A Labor Ministry source said that as of late November, his ministry had yet to complete translating into Thai the text presented by the U.S. in the October FTA round.

19. (SBU) But like the elections, we don't accept that the need for greater preparation time is the major reason for the postponement. Only a minority of the negotiating groups were faced with serious preparation related obstacles that would, arguably, delay further meetings. Preparation for 90 percent of the negotiating groups would have been advanced by the December talks, since the talks would have provided opportunities for information exchange, clarification of positions, and so forth. It is evident that factors other than the need for additional time for preparation played a role in the postponement.

#### "REQUEST SHOCK"

10. (SBU) While the RTG thought that it had done its homework in preparation for the FTA talks with the U.S., it has found out that much more remains to be done. The RTG -- or at least many of its key officials -- were seemingly caught off guard by the scope and depth of U.S. requests in many areas. These areas include labor; environment; financial services. When we express our astonishment to RTG officials at their surprise at the U.S. agenda (after all, the U.S. must rank as the most transparent country in the world in terms of negotiating goals in our trade relations -- our complete negotiating agenda has been available on the Internet for several months prior to the start of negotiations), they respond that 1) the full impact and ramifications of the U.S. requests had not been fully appreciated; and 2) not all RTG officials had been fully briefed in advance on the U.S. negotiating position. A prominent official that probably falls into this category is the Prime Minister; while he is a supporter of an FTA with the U.S. -- indeed, he claims authorship of the idea -- he is probably unaware of what its contents are likely to be. All indications are that he has been caught off guard by the

overall U.S. request list, and is disappointed that the U.S. is unwilling to negotiate a quick and politically attractive "early harvest" package. (Note: We believe the RTG's "early harvest" plan for the FTA with the U.S. largely involved formally renewing key provisions (Articles 4 and 10) of the U.S.-Thailand Treaty of Amity and Economic Relations.)

#### "LITTLE DEALS WITH BIG COUNTRIES"

11. (SBU) Seen through Thai eyes, the U.S. requests suffer from comparison with the other recent trade deals Thailand has concluded. Many of these deals lack (at least for now) comprehensive market opening substance, opting instead for relatively easy "early harvests." This is the case for both China and India. Even the FTA with Australia is fairly slow-pitch: aside from reductions in goods tariffs, very little was accomplished. By comparison, the breadth of the FTA with the U.S. is wildly ambitious -- maybe too ambitious for some. One knowledgeable local observer said, "Thaksin wants little deals with big countries; they make good headlines without causing too much trouble."

#### "OFFER SHOCK"

12. (SBU) The RTG has also had to review its strong desire for a temporary entry chapter (or at least strong temporary entry provisions as part of a services chapter) in the FTA. The desire for a U.S. visa is strong in Thailand (the U.S. has long been the country of choice for education, for example); one of the strongest appeals of the U.S.-Thailand Treaty of Amity and Economic Relations are the reciprocal preferential visa provisions. We believe the RTG has been counting on reaffirming and perhaps upgrading this provision as a big part of its public sales campaign for the FTA. Adding insult to injury is the inclusion of temporary entry chapters in the Chile and -- most importantly -- Singapore FTAs. Thailand's rivalry with the latter country is an important reason behind the RTG's persistence in asking for temporary entry provisions. Lead Thai negotiator Nitya recently cited the temporary entry provisions negotiated in the U.S. FTA with Singapore in wondering aloud to the Ambassador whether an FTA without temporary entry provisions would be acceptable to the RTG. He said, "Of course, it isn't my call, but you know what the Old Colonel (PM Thaksin) thinks about Singapore." We believe the RTG's basic position on somehow addressing temporary entry is inflexible, and as such is probably one of a handful of issues that falls outside the normal give and take of the negotiating process. In the absence of some treatment of temporary entry in some context (not necessarily within the FTA), we question whether the RTG will agree to an FTA.

13. (SBU) The RTG hopes that the post-U.S. election climate will be more amenable to the discussion of temporary entry. In noting that the President's party has strengthened its majority in Congress, some officials here are hopeful that the U.S. may re-think its position on temporary entry and trade agreements. In arguing for a delay in further FTA talks, the Prime Minister's chief economic adviser, Dr. Pansak Vanyaratyn, asked the Embassy's Economic Counselor, "Why don't we wait until both of our governments have a mandate?" The "mandate" Pansak probably was referring to in the case of the U.S. was a reconsideration of our position on excluding temporary entry from trade agreements.

#### PRIVATE SECTOR OPPOSITION

14. (SBU) The corporate elites of Thai society are viewed by many here as highly insecure. "They don't see any opportunities in liberalization, only the loss of privilege," one source told us. While there is considerable truth in this statement, we think it is somewhat exaggerated; in reality, private views are mixed. In general, the Federation of Thai Industry (which accounts for much of the manufacturing sector here) generally is supportive of the FTA. Opposition to the FTA is centered in the Thai Bankers Association and large swathes of the Thai Chamber of Commerce. These are powerful organizations, and they no doubt have made their voices heard.

#### INTER-MINISTERIAL CONFLICT

15. (SBU) Long simmering differences over policy and jurisdiction boiled over in the November 21 FTA Oversight Committee meeting that called for the December round's postponement. Far from being resolved, these differences could become sharper in the coming months. Normally (and by law), trade negotiations are led by the Ministry of Commerce. For the U.S. FTA, the Foreign Ministry has the lead. Lead Thai FTA negotiator Nitya has the title of Adviser to the Foreign Minister. This is not a very powerful position. The Chair of the FTA Oversight Committee is Finance Minister Somkid. Somkid is a politically powerful Cabinet minister (a coterie of MPs owe him allegiance); he is thought to be a leading proponent of the skeptical, "go-slow" school

regarding the FTA with the U.S., favoring a narrow agenda that focuses on traditional market access issues. His major ally on the FTA Oversight Committee is Dr. Pansak. This pair have found common cause in blocking Nitya's plans for the FTA, which included the December negotiating round. Nitya (allied with FM Surakiart) favors a full speed ahead, comprehensive FTA agenda. In terms of both institutional and personal political power, this pair easily outguns Nitya. This intra-governmental conflict could continue -- and even worsen -- beyond the February elections.

16. (SBU) At the inaugural November 22 meeting of the RTG's newly created FTA Oversight Committee, the various themes of the several dissenting factions -- those concerned over the elections, inadequate preparations, "request shock", or "offer shock," -- came together, finding common cause in a call to stop forward progress on the FTA pending a reassessment of the entire FTA exercise. Most observers here think the FTA talks will be re-started after the elections, but such an eventuality awaits a formal decision to that effect by the FTA Oversight Committee.

#### POSSIBLE FUTURE DEVELOPMENTS

17. (SBU) Frustrated by the proliferation of ill-informed FTA oversight committees (we currently count four that play some role in the FTA) and his inability to chart the course of the FTA talks, Nitya is lobbying to be given the title of Thai Trade Representative. This can be designated a Cabinet level position, and would give him a fighting chance of regaining control over the FTA agenda. We understand a decision regarding this is not likely until after the elections. Everyone here thinks that Thaksin's Thai Rak Thai party and its allies will win handily, probably increasing their majority in the lower house of parliament. If the post-election Minister of Commerce is a politically powerful figure, it is possible that Commerce may seek to assert its leadership in the U.S.-Thai FTA talks. In that case, Commerce probably would resist increasing Nitya's power, and the latter could find his position untenable. But, while a Commerce takeover of the talks could spell trouble for Nitya, it might not be all bad for the FTA; what is needed to drive negotiations forward is 1) strong commitment 2) from a powerful figure. A new Commerce Minister might prove just the ticket. In this regard, we find it significant that the Commerce-led FTA talks with both India and China continue to move forward, while the MFA-led FTA talks with the U.S. and Japan have been delayed.

18. (SBU) Somkid and Pansak are thought to be dissatisfied with both the U.S. negotiating framework and (derivatively) proposed pace of the FTA negotiations. Somkid (seconded by Pansak) has described the negotiating mandate set forth in U.S. Trade Promotion Authority legislation as negotiating "pre-conditions," (they count 17 such TPA pre-conditions in total) and as such undermine the RTG's desire for both sides to negotiate from a clean slate. They also object (in varying degrees) to various U.S. positions (as cited in paras 10-12). Their initial response has been to halt the talks, albeit temporarily. Somkid and Pansak surely have the support of PM Thaksin, at least for now. Said one long time Thai observer, "This is a classic Thai response to being pushed faster or farther than they want to go; they step back."

19. (SBU) But the temporary delay is only a tactical move; we think major strategic decisions have been deferred until after the February elections. Foreign Minister Surakiart recently told the Ambassador, "We have a mandate to pursue these talks after the elections," and vowed to resume talks once "the necessary parliamentary and legal processes are complete." Surakiart added that he had made these points to U.S. Trade Representative Zoellick during the recent APEC meeting in Santiago, Chile. The full speed ahead school, which includes FM Surakiart, have been arguing that with the proliferation of FTAs, the costs of non-participation are likely to be very high.

20. (SBU) In a separate meeting with the Ambassador, Finance Minister Somkid was somewhat less encouraging, telling the Ambassador, "We will not do anything we cannot explain to the Thai people. After the elections, we will meet with our entire FTA team and look at every position; I think we can handle everything." He then made an indirect pitch for an "early harvest" approach: he described a meeting he had with the lead Japanese FTA negotiator, where he had urged the Japanese to consider immediate FTA concessions, leaving other areas for later. He concluded by saying, "We need to be careful. Many in Thai society are ready to be opposed to an FTA with the U.S. We don't want to let that happen." While he didn't spell out exactly how he proposed to avoid such an eventuality, the overall message seemed to be, "Go slow, be moderate in your requests."

21. (SBU) We find it significant that no RTG official has told us they are opposed to the FTA per se. The opposition

for now seems mostly short term and tactical. We think there is a good chance that even hard core opponents of Nitya, such as Pansak, may change their tune after the elections; in Pansak's economic writings, he touts the modernizing effect of FTAs. Whatever its short term political advantages may be, a narrow market access type of FTA will not yield much in the way of economic modernization.

#### WHAT WE SHOULD DO

122. (SBU) While it is easy to be discouraged by some of the attitudes toward the FTA that are prevalent here, we see the current hiatus as a temporary setback that in no way alters the overall situation. A Free Trade Agreement with Thailand clearly remains in our interest. Usually, an FTA is designed to take bilateral relations to a new level. In the case of Thailand, however, much of our motivation is the preservation of our current position. The U.S. currently is Thailand's largest trading partner. In investment, U.S. firms have privileged access to the Thai market under the Treaty of Amity and Economic Relations (AER). But our status is imminently threatened by current trends. In view of GATS MFN issues, we doubt the AER has much of a future as a stand-alone document. The relentless rise of China's economic profile in this region represents a challenge to the U.S.'s trade and investment leadership. Additionally, Thailand is negotiating a number of other FTAs, which probably will create some trade diversion that disadvantages U.S. exporters. Given these developments, without a new framework for our commercial relationship we will find it a challenge to maintain our current position.

123. (SBU) We also think pursuing an FTA is the right thing to do for reasons that go beyond maintaining our position here. A close precedent to what we are trying to accomplish with our FTA with Thailand is the Mexico component of NAFTA. Like Mexico, Thailand is a medium-sized developing economy. Like Mexico, Thailand is essentially not a rules-based economy, relying, instead, to a great extent on personal, informal arrangements. As envisioned by the U.S., our FTA with Thailand will effect a transformation within the Thai economy, by moving it towards a more rules-based, transparent way of conducting commerce. Such a transformation will be hard to achieve; it will be much harder than anything Thailand is likely to ask the U.S. to do. It is also a safe bet that, similar to the case with Mexico, that a comprehensive FTA will see Thailand make the vast majority of the concessions, since the vast majority of the existing trade and investment barriers are on the Thai side. Leading RTG policy makers are aware of the transformational, modernizing potential of the FTA and, in their more visionary moments, cite that potential as the FTA's chief attraction. But, it is an open question whether the Thai Government or people are willing and capable of effecting such a transformation. The chief architect of PM Thaksin's economic plan ("Thaksinomics"), Pansak Vanyaratyn, wrote, "I am not sure we have the iron will to stay the course. I am not certain that we, meaning, the Thai State or the Thai private sector, have the will or the stamina to complete the change that we have set in motion." We share Dr. Pansak's uncertainty.

124. (SBU) While posing great challenges, the transformational potential of an FTA with Thailand is what makes it worthy of great effort on our part. By helping Thailand move toward more rules-based, transparent, and efficient governance, an FTA with the U.S. will be the catalyst for much higher output and living standards in Thailand. It will be a world showcase, serving as a positive precedent for the many other developing economies which are weighing economic development and trade policy options.

125. (SBU) Deciding on the future course of the FTA is largely a Thai question which eventually will be resolved by a debate within the Thai Government and society. Our opportunity for input is limited. As far as the U.S. management of the FTA negotiations goes, we don't have a lot of fine tuning to recommend since there are few, if any, complaints in this area. On the contrary, Amb. Nitya has on several occasions publicly expressed his appreciation for the professionalism of the lead USTR negotiator.

#### EMPHASIS ON SMEs COULD HELP

126. (SBU) The Thaksin Government has placed a heavy emphasis on small and medium sized businesses. Following the 1997 economic crisis, the RTG believed that the potential in SMEs and the traditional sector, given its great flexibility, diversity, and low import content, would provide a new source of economic growth and income. The RTG has introduced a host of economic programs aimed at boosting this sector of the Thai economy, which already accounts for almost 40 percent of Thailand's GDP. This sector also represents a core constituency of Thaksin's Thai Rak Thai party.

126. (SBU) Our FTA framework could be more attractive to the



RTG if there was a greater emphasis on SMEs across the various negotiating groups. This would mainly involve changes in formatting and emphasis, not new concessions. RTG officials point out that an FTA that could be marketed in Thailand as an "SME FTA" would be a much easier sell to Thai public opinion (and would be much more attractive to PM Thaksin, whose exact position on the RTG's internal FTA debate remains uncertain). Our nascent "Group on Small and Medium Enterprises and Other Cooperation" represents a good start; it is possible that other opportunities to emphasize SMEs could be identified and exploited in other negotiating areas. For example, in the government procurement chapter it might be possible to highlight the small business set-aside provisions, and gear our efforts in trade capacity building toward this area. It might be possible to enlist the aid of the U.S. Small Business Administration on this project.

27. (SBU) In spite of the delay and internal RTG soul-searching, we remain basically optimistic about the FTA's prospects because we don't see how anyone's fundamental interests in having an FTA have changed. It is overwhelmingly in Thailand's interest to have an FTA with the U.S., whether one argues on the grounds of its transformational, modernizing effect; the high costs of non-participation; market access; strategic alliances; or some combination of these. An FTA with Thailand remains overwhelmingly in our interest, whether one argues on the grounds of maintaining our strong position here; the hugely beneficial transformational effects in the Thai economy likely to accrue from the FTA; or the demonstration effect on other developing economies. In asking for a comprehensive, transformational FTA with the U.S., we are asking Thailand to do something unprecedented, something that it will find very hard. Negotiations are likely to take some time. Progress might be non-linear, with periods of rapid movement forward, followed by some regression, a hiatus, and a repetition of this cycle. It will require patience, determination, and judgment, with no guarantee of success. But we believe it is worth the considerable effort likely to be required.

JOHNSON